

Before the
Federal Communications Commission
Washington, D.C. 20054

In the Matter of)	
)	
Implementation of Section 621(a)(1) of)	
the Cable Communications Policy Act of)	MB Docket No. 05-311
1984 as amended by the Cable)	
Television Consumer Protection and)	
Competition Act of 1992		

REPLY COMMENTS OF BROADBAND SERVICE PROVIDERS ASSOCIATION

The Broadband Service Providers Association (“BSPA”) hereby submits its reply comments in the captioned proceeding.¹

EXECUTIVE SUMMARY

The BSPA offers the following summary comments.

1. Existing competitive franchises should not be used as models for what has historically worked and they should not be used as models for future franchise process. These franchises were negotiated under distorted and invalid market conditions that inflated the perceived value of a new competitive franchise.

¹ *Matter of Implementation of Section 621(a)(1) of the Cable Communications Policy Act of 1984 as amended by the Cable Television Consumer Protection and Competition Act of 1992*, Notice of Proposed Rulemaking, MB Docket No. 05-311, FCC 05-189 (rel. Nov. 18, 2005) (“NPRM”).

2. Legacy “Level Playing Field” statutes have actually impaired the development of competition and resulted in lawsuits to forestall the development of competition.
3. Any franchise reform needs to fairly address all business and investment models that can bring competition and consumer choice to the market.

INTRODUCTION AND BACKGROUND

BSPA represents competitive network operators that have significant experience with existing cable franchising regulations. The BSPA was formed in 2002 to represent a new segment of the communications industry that emerged following passage of the Telecommunications Act of 1996 (“1996 Act”). Broadband service providers (“BSPs”) deploy and operate new, facilities-based, advanced, last-mile broadband networks for the delivery of innovative bundles of voice, multichannel/on-demand video, and high-speed data/Internet services directly to homes and small businesses across the country.² While today’s BSPs represent a smaller segment of the industry -- over forty networks that serve more than 1.2 million customers -- they have achieved significant market share where they operate. These networks represent over 133 competitive franchises that have been negotiated under the current rules and regulations.

² The current members of BSPA, all of which are last-mile, facilities-based providers, are: Everest Connections, Knology, Sigecom Communications, PrairieWave Communications, and SureWest Communications.

BSPs provided the first working examples of competitive next generation integrated systems. These are the system structures that cable and telephone incumbents are now rebuilding and upgrading their networks to provide similar capabilities. From a new entrant's standpoint, BSPs have experienced the full range of competitive responses that other new distribution entrants are facing today in the deployment of competitive networks. Thus, the market experience of BSPs provide important insights into the competitive issues that must be addressed by the FCC and Congress for promoting and evaluating head-to-head facilities-based competition that will create the most effective market structure to serve consumers and ensure economic growth.

DISCUSSION

I. Perspectives on Existing Competitive and Incumbent Cable Franchises.

Many comments filed in this proceeding have referred to existing competitive franchises. Comments filed by LFAs have typically described these historical competitive franchises as models of success on how the existing regulatory structure has functioned. While these franchises exist, the treatment as models for either success or future franchise process should not occur. Most of these legacy competitive franchises were negotiated with BSPs in the middle to late 1990's at a time when the market has now been characterized by the phrase "irrational exuberance".

After passage of the 1996 Telecommunications Act there were significantly inflated perceptions regarding the expected value creation by new competitive or upgraded cable networks. At the time AT&T was creating perceived network values by purchasing non-upgraded cable systems for over \$3,500 per subscriber. Multiple new entrants, funded with significant venture capital, were competing for new competitive franchises. Their competition with each other contributed to a form of unrealistic bidding where the LFAs were in a position to successfully request expanded economic incentives tied to granting the competitive franchise. In some cases these provisions actually exceeded the provisions of the incumbent's franchise with payment under the new competitive franchise contingent on the same provisions being ratified as part of the renewal process for the incumbent. These requirements were more burdensome on new entrants since unlike the incumbents there were no existing revenue streams to fund the obligation.

The specific provisions of a franchise were public domain and other LFAs would often use an existing new competitive franchise as the model for the minimum contributions that would be expected as part of their franchise negotiations. New entrants could experience a fairly quick process to complete a franchise assuming ready agreement to all of the provisions of a "model" franchise that had been negotiated by another LFA during this period of "irrational exuberance". Third party consultants also emerged to represent

LFAs in the negotiation process representing the LFA(s) with the goal of maximizing the economic value a LFA could extract from the franchise process.

The real issue is that the terms and conditions of these early franchises were and are not justified by the real economics of the network investment. When AT&T merged with Comcast, AT&T suffered an enormous write down of value for that very reason. The most recent valuations for fully deployed and upgraded triple play competitive networks have had a value range of approximately \$1,200 to \$2,000 per cable subscriber. Competitive triple play networks have demonstrated economic viability but they do not produce the original values assumed when the early franchises were negotiated.

The “triple play” networks as opposed to satellite networks have demonstrated the significant value of full wireline competition in the territories they serve. Wireline competition lowers prices and expands services. Competition and the expansion of services are the core benefits brought by new entrants. The creation of new community services or revenues for LFAs that are financially absorbed by the competitive system operator do not achieve those benefits. Excessive fees, requirements, restrictions, and lengthy negotiations in the franchise process only delay or forestall investment and the consumer and economic value that full competition brings to the marketplace.

It should also be noted that this might be the first time in cable industry history that incumbent cable operators have talked about the inherent fairness of and have offered support for the current Franchise regulations. In light of

this history, it is difficult to understand their new position as anything other than a desire to use the process as barrier of entry to delay or impair competition. There is a long history of transactions for incumbent cable companies where limited partnerships have been used to allow investments to be completed without franchise transfer thus avoiding the franchise process. There is also significant history of incumbent cable companies not negotiating renewal franchises in a timely manner. At the time of the Comcast/AT&T merger, petitions were filed by LFAs requesting that the merger be denied until all of the outstanding defaulted franchises were negotiated and renewed.

This history creates a compelling profile that the current Franchise process has not been completely effective or efficient. The current regulations leave too many issues subject to open-ended negotiations where the LFAs could try to extract as much value as they can from issuing a franchise using benchmarks from competitive franchise provisions agreed to during a time period of irrational market values and unjustified economic burdens required of new investments. The only way to effectively break this cycle is to more clearly define the obligations and contributions that are justified for an MVPD network operator to provide to an LFA and apply them to each operator, incumbent or new, on a per subscriber basis as historically has been done with franchise fees. Obligations that need to be addressed with clear boundaries include, but are not limited by INET, PEG Channels, and any PEG support fees.

II. Level Playing Field Provisions and Associated Build-out Requirements Are Significant Impediments to Competition.

Level Playing Field Provisions provide an additional opportunity to use the franchise process as an impediment to competition. The definition of what constitutes a “level playing field” is also not clearly defined. Incumbent cable operators will define level playing field to include any and all accumulated payments or franchise requirements that have historically been complied with. In this regard they seek to impose conditions that were the result of many years operating as a sole licensee whereby most fees and obligations were funded out of operations, rather than funded by diverting capital funds in order to gain franchise approval.

The single largest issue in today’s video franchising regime is build-out requirements that exist as a level playing field (“LPF”) statute or similar requirement in an incumbent’s heretofore monopoly franchise agreement. Build-out requirements do not create a true level playing field. Build-out requirements may have been appropriate when an exclusive franchise was being issued, but they have no place in a competitive market. They primarily serve to delay or limit the growth of competition by negatively impacting the availability or use of capital.

For example, an LPF suit was brought by Insight Communications against the City of Louisville and Knology. Litigation in this matter took more than three years. The City of Louisville and Knology eventually won the suit, but the case was settled with no damage award. More importantly, the extensive delay resulted in

Knology pursuing other market investments and declining to enter the Louisville market. Thus the suit was an excellent competitive investment by Insight since full wireline competition has still not emerged in Louisville because of the incumbent's strategic use of litigation over a LPF provision.

Knology approached the city of Louisville, Kentucky in early 2000 and applied to obtain a cable television franchise. Knology considered this market to be an excellent opportunity because it believed the incumbent provider's (Insight's) network and operations lagged behind industry norms. Knology believed that if it could enter quickly on competitively favorable terms, it could capture a large share of the customer base by offering more services at better prices. The initial informal discussions with the city were promising, but, because the incumbent cable provider's agreement had a LPF provision, the negotiations quickly became much more complicated. The city was particularly concerned that it would be sued by Insight, which would be a costly procedure to defend its actions.

Because of the LPF provision, the city sought to draft an agreement as identical as possible to the incumbent's. Each time a new draft was produced, the city would share it with the incumbent. Each time the incumbent would respond with another set of revisions.

Four issues were most prominent. First, Insight was required to pay the City \$500,000 in five annual installments as part of a settlement arising out of the overcharging of cable customers in the 1980s. As part of the settlement agreement, however, this obligation was also incorporated into Insight's cable franchise.

Insight insisted that Knology be required to make the same payments so its franchise would not be “more beneficial” than Insight’s. Knology acceded to this blatantly unfair demand in order to get a franchise and required Knology to make its first payment at the moment the franchise was granted despite the fact that Knology would have no network, customers or cash flow. Second, Knology sought a 15-year franchise, which was the same duration as the initial franchise of the cable operator that was acquired by Insight. The incumbent argued that the term of the franchise should be 10 years, the same term in its renewed franchise agreement. Third, Insight argued that it was able to rebuild the previous cable operator’s network in 15 months, and Knology, despite being a new entrant, should have a similar requirement for its new network construction. Insight also argued that Knology should have additional bonding requirements to cover any cable cuts and should suffer severe penalties if it did not meet the build out requirements. (Neither of these requirements were in Insight’s agreement.) Fourth, Insight alleged Knology was not financially fit, which resulted in the city hiring a consultant to review Knology’s financial wherewithal.

Because these issues were so contentious, the process dragged on. It was not until September 2000 that the city approved the franchise by a vote of 7-5. This, however and most unfortunately, was not the end of the process. Insight’s agreement permitted it to delay the implementation of any new franchise until all appeals to the highest court in the state were completed. Thus, began another round of delay as Insight took the city’s decision to court.

These delays enabled Insight to upgrade its network, improve its operations, and enter into exclusive agreements with owners of multiple dwelling units. As a result, Knology's market opportunity evaporated, and it never entered the Louisville market.

New networks also derive significant revenues from telephone services, but there are distinct differences between the local requirements that may be imposed on the provision of competitive telephone service and the ability to offer competitive video services. Compared to the local video franchising process, there are only limited regulatory impediments to a facilities-based operator offering voice services. Therefore, incumbent cable operators can offer new competitive phone service through network upgrades in any geographic manner or market, without input or oversight by local governmental authorities. In contrast, both legacy phone companies and new network operators face significant and daunting obstacles to the provision of video services arising from the local franchising process and its associated requirements.

III. Any Changes to the Franchising Process Must Apply to Current competitive Operators and potential New Entrants.

Franchising reform needs to address all market positions and technologies that bring competition and consumer choice. Many filed comments most clearly related to the position of telephone companies and their desire to upgrade existing systems to offer video services. We recognize the need to address the unique circumstances of these proposed investments but also offer the

perspective that incumbent telephone companies will not bring all of the competition desired by the market in a timely manner. Many markets will be first served by new network construction more typical of the historical BSP model than a model based on the upgrade of an existing network. There are also significant opportunities for existing competitive networks to expand competition through network extensions into adjacent territories with additional new construction that is not based on any pre-existing presence in the right-of-way. The regulatory goal needs to be equal opportunity for all forms of business models and technology. In addition to market expansion, it is also likely that new entrants building new networks will provide a significant level of innovation that the industry will benefit from. We therefore re-emphasize that the commission needs to fully consider all of the following competitive positions in the MVPD market.

1. Existing networks that want to upgrade service.
2. The construction of new networks regardless of the chosen technology.
3. The expansion of existing competitive networks with additional new construction.
4. The position of current competitive franchises that may exist under franchise provisions that could be burdensome or disadvantaged as compared to competitive franchises issued under new rules.

All of these market positions need to be fairly addressed to provide the foundation for the greatest expansion of desired competition. New franchise

rules should not determine which of these competitive business models should win or lose.

CONCLUSION

The BSPA continues to endorse the expansion of competition and consumer choice in the MVPD market place. Franchise reform can lead to the additional expansion of competition and will be most effective if those reforms have fair application to all technologies and potential business models that can bring competition.

Respectfully submitted,

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